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IN THE
Supreme Court of the United States.

OCTOBER TERM, 1896.

SOUTHERN RAILWAY COMPANY,
Appellant,

vs.

CARNEGIE STEEL COMPANY (LIMITED),
Appellee.

Petition of Appellant for a Writ of Certiorari to
the U. S. Circuit Court of Appeals for
the Fourth Circuit.

HENRY CRAWFORD,
WILLIS B. SMITH,
Solicitors.

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In the Supreme Court of the United States.

OCTOBER TERM, 1896.

SOUTHERN RAILWAY COMPANY,

APPELLANT,

VS.

CARNEGIE STEEL COMPANY (LIMITED),

APPELLEE.

Petition of the Southern Railway Company for a writ of certiorari to bring up the decree of the Circuit Court of Appeals for the Fourth Circuit.

TO THE HONORABLE JUDGES OF THE SUPREME COURT OF
THE UNITED STATES :

Your petitioner, the Southern Railway Company, respectfully shows to the Court as follows :

On June 16, 1892, in a suit brought by William P. Clyde and others, general creditors, alleging insolvency, the Circuit Court of the United States for the Eastern District of Virginia appointed Receivers of all the Richmond and Danville Railroad system.

The only railroad it owned was its charter line from Richmond to Danville, in Virginia. It also leased, operated and controlled as a part of its system a large number of railroads in Virginia, North Carolina, South Carolina, Georgia, Alabama and Mississippi and the District of Columbia.

The order appointing the Receivers directed them to continue to operate all the leased lines until the Court should order otherwise.

It also required them to pay, as preferential charges, out of the current earnings, all pay-rolls and operating supply vouchers incurred within six months prior to their appointment.

By subsequent order, on June 28th, 1892, \$1,000,000 Receivers' first-lien certificates were issued, and the proceeds used to pay such ante-receivership six months' debts.

The order made such certificates a lien on the railroad prior to all mortgages, and was in express terms allowed, for the purpose of enabling the Receivers to use their current income to pay rentals on the leased lines.

No motion was ever made by any creditor to modify either of such orders.

On August 16th, 1892, Special Masters were appointed to take proof of corporate debts.

The railroad company had previously executed three mortgages to secure \$6,000,000 first, \$4,000,000 debenture and \$4,527,000 consolidated bonds, respectively.

None of these mortgagees were parties to the Clyde suit when brought and neither of such liens was then in default.

The consolidated mortgage was executed October 22, 1886, to the Central Trust Company of New York. It covered the owned road from Richmond to Danville, its estate in the Piedmont Railroad in North Carolina and its leaseholds or rights under operating contracts with the York River, North Carolina, Atlanta Air Line, Virginia Midland, Western North Carolina, Charlotte, Columbia and Augusta, and Columbia and Greenville Railroads. Also all such first mortgage bonds issued by other railroad companies, thereafter leased or acquired by the mortgagor, which might be deposited with the mortgagee, and all such Richmond and Danville debenture bonds secured by its mortgage of 1882 as should be deposited in exchange for consolidated bonds.

The final decree finds that \$4,527,000 of consolidated bonds had been issued for value. Of these \$1,351,000 were in exchange for deposited debenture bonds, \$350,000 were for equipment, \$2,826,000 were to acquire \$2,854,000 first mortgage bonds of the several independent roads, as specified. Such debenture and mortgage bonds of third companies were lodged with the trustee and constituted an important part of the security covered by the consolidated mortgage.

On October 14, 1892, the Carnegie Steel Company (Limited) filed with the special Masters in the general receivership suit a claim upon five notes executed by the defendant Railroad Company for rails sold.

No claim of lien or preference was made.

By amendment of February 24, 1894, it alleged that by reason of a wrongful diversion of earnings to the payment of bonded interest the claim was entitled to an equitable preference over the consolidated mortgage then in process of foreclosure.

By an amendment of March 12, 1894, it was also alleged that, under Section 2485 of the Code of Virginia, the claim was a prior statutory lien upon the franchises, gross earnings, real and personal property of the defendant railroad company.

This debt arose under a written contract executed June 10, 1891, between the steel company and the mortgagor railroad. The latter agreed to buy steel rails for \$30 a ton payable in the buyer's notes at four months, without interest, with a debtor privilege of two additional renewals of three months each.

The rails were to be delivered to the purchaser in Pennsylvania and there was no recital or covenant whereby they were to be laid on any particular road in the six States wherein the owned, leased and operated system was situate.

The uncontradicted testimony was, that of the total deliveries of 4,203 tons, only about 175 tons were actually laid in the railroad between Richmond and Danville. The remainder were laid in other roads in Georgia, North Carolina, Virginia, Alabama and Mississippi.

The outstanding notes evidencing the claim aggregated \$125,067.39 matured after the receivership and were second, third and fourth renewals of the original paper.

No interest was paid upon the debenture or the consolidated mortgage bonds at any time during the Receivership or foreclosure. All interest paid upon senior main-line and branch bonds was paid under Court orders requiring such payment, to which no creditor objected.

In July, 1893, the Central Trust Company brought sought to foreclose the consolidated mortgage.

On the mortgagee's motion, the Court appointed a new set of Receivers, and ordered those appointed June, 1892, in the general creditors' suit to surrender possession. The mortgagee Receivers were to take over the assets and balances of the original Receivers, and were required to pay all their just debts and liabilities.

On the closing of the accounts of the original receivership there was a net deficit of several hundred thousand dollars which was assumed and paid out of the income received by the mortgagee receivership.

In the foreclosure suit the Court made no fresh order as to the appropriation of income to preferential claims, except that it was provided that "nothing in this order contained shall be construed to vacate any of the orders heretofore entered in the case of William P. Clyde and others, but the Court reserves full power to act upon the Master's report, filed in the said cause, and in said cause to adjudge and decree upon the rights of creditors asserting a claim against the property of the said railroad company or income thereof in preference to the mortgage debt thereof by orders to be entered in the said suit of William P. Clyde and others upon notice to parties, with like effect upon the mortgage property and income, as if the orders were entered in this cause."

At that time the orders of record in the Clyde suit expressly required the payment of the rental on leased lines by the Receivers and restricted any preference against earnings to such claims as were incurred within the six months immediately preceding the first Receivership.

No creditor had ever moved to enlarge that limit, and no claim for any preference was filed by the steel

company until long after the foreclosure suit was brought.

On February 17, 1894, on the application of the appellee, the original Receivership suit was consolidated with the foreclosure action.

During the mortgagee's receivership, the foreclosing consolidated bondholders received no interest. The total earnings were not nearly sufficient to meet the operating expenses and interest on prior bonds. The deficit was paid out of the sale proceeds.

In April, 1894, a final decree was entered foreclosing the consolidated mortgage and ordering the sale in one parcel of all the railroad, leaseholds, contract rights and deposited securities.

Power was therein reserved to order the purchaser to pay all claims which it should thereafter "adjudge to be prior in lien or superior in equity to the mortgage foreclosed in this suit."

All the mortgaged railroad and other property was sold as a unit to the petitioner for the sum of \$2,020,000.

The sale was confirmed, conveyance executed and the petitioner let into possession.

In May, 1894, the Special Masters filed their report upon the intervention of the steel company.

They found that the claim was not entitled to any equitable preference upon the Receiver's income or the railroad, but that under the Virginia Code it was a statutory lien upon the sale proceeds prior to \$2,906,000, but subordinate to \$1,621,000 consolidated bonds.

Both parties excepted.

The Circuit Court on final hearing allowed a decree, finding that the railroad company owed the appellee \$125,067.39 principal and \$29,828.58 interest for steel rails sold and adjudging that the steel company, under

the statutes of Virginia, was entitled to a priority of payment out of the sale proceeds over \$2,906,000 of the consolidated bonds; also, that the receivership earnings, which should have been used for the payment of current expenses, including the claim of appellee, had been used for the benefit of mortgage creditors in a sum more than sufficient to pay such claim, and consequently was entitled to prior payment out of the sale proceeds over the entire issue of consolidated bonds.

The purchaser was therefore ordered to forthwith pay the appellee the sum of \$154,895.97 for principal and interest of its debt.

The purchaser took an appeal from this decree to the Circuit Court of Appeals for the Fourth Circuit.

The latter Court, while expressing no set opinion as to the effect of the Virginia statute, has now entered a decree affirming generally the decree of the Circuit Court, and appellant is required to pay the entire claim of the Steel Company together with interest to the date of payment.

Petitioner submits the following reasons why the said decree of affirmance should be brought here for review by this Court:

FIRST. The questions of law involved in the affirmed decree are of general importance and interest because they materially concern the recorded priorities of mortgage bondholders upon all railway property, and if allowed to remain as an unchallenged precedent will of necessity govern future decrees of foreclosure in such Circuit and elsewhere, and determine that unsecured floating debt creditors are entitled to full payment out of the proceeds of mortgaged railways

in preference to the vested contract liens of the recorded mortgagees.

SECOND. As affecting all railway property and interests therein it is of general importance to have it authoritatively decided whether after the several States have enacted valid laws creating and fixing the rank of liens upon railway property and earnings, it is competent for the Courts of the United States to allow and enforce discretionary liens thereon, which in effect abrogate such State laws and deny to these interested the rights and priorities expressly vested in them by valid statutes.

THIRD. It is of general importance that the rights and liens of mortgage bondholders upon railways in respect to claims of unsecured creditors asserting equitable priority upon earnings and sale proceeds should be determined by uniform decision so that such important interests and liens should not be rendered insecure or doubtful because of the conflicting rulings of different courts of equal authority.

The opinion and decree of affirmance involved in this application is in direct conflict with the rulings of other courts of appeal and with its own previous decision.

Unless corrected by the action of this Court its present attitude will unsettle the established principles now applicable to such property.

FOURTH. The Circuit Court of Appeals failed to follow or give force or effect to the ruling and decision of this Court on the legal proposition involved, in that it erroneously decided and decreed that mortgage bond-

holders when they came to foreclose their lien ought in equity to be charged with payments made and the acts and results of a receivership obtained in a general creditor's suit when the mortgagee did not apply, and his security was not in default and he personally received no interest during such receivership.

FIFTH. The Circuit Court of Appeals failed to follow or to give force or effect to the rulings and decision of this Court on the legal proposition involved, in that it erroneously decided and decreed that the claim of a large manufacturer for \$125,000 of rails sold and delivered in Pennsylvania two years before the mortgagees' receivership on extended optional credit of at least ten months, was a creditor of the current receivership income for necessary operating supplies, or entitled to an account thereof and restitution of sums paid for interest and necessary rentals under unimpeached Court orders.

SIXTH. The Circuit Court of Appeals failed to follow or give any force and effect to the rulings and decisions of this Court on the legal proposition involved, in that it erroneously decided and decreed that interest paid upon senior mortgages during a receivership obtained by general creditors, constituted an inequitable diversion by the junior consolidated bondholders who subsequently sued to foreclose, so that the sale proceeds of their own mortgage security could be rightly taken to make restoration to the fund for unsecured creditors.

SEVENTH. The Circuit Court of Appeals erroneously decided that there had been diversion of the original receivership income as against the rights of the steel

company, and that payments made by the Court officers, under its express orders, were in law chargeable upon the security of the consolidated mortgage bondholders, and should in law be first paid out of the proceeds of foreclosure sale.

EIGHTH. As the entire mortgaged property, embracing not only the railroad, but all the \$2,844,000 of first mortgage bonds of independent railroads on which appellee had no possible lien, was sold for only \$2,020,000, and the Circuit Court decreed that the claim of the steel company was a lien under the statutes of Virginia upon the railroad and earnings inferior and subordinate to \$1,621,000 of the bonds issued under the consolidated mortgage, upon which decree the steel company failed to assign error or appeal, and which has been affirmed by the Circuit Court of Appeals, both said Courts decided erroneously in ordering payment of any part of the intervenor's claim, because they deprived the \$1,621,000 bonds and interest thereon of the statutory priority which had been expressly decreed to them out of the net proceeds of sale which were insufficient to pay them in full.

NINTH. The Circuit Court of Appeals decided erroneously and contrary to settled legal principles in affirming the decree of the Circuit Court which split the lien and priority of a single recorded mortgage securing negotiable bonds and discriminated between the bonds protected thereby in consequence of the separate date of their original issue.

TENTH. The Circuit Court of Appeals decided errone-

ously and contrary to settled legal principles in affirming the decree that steel rails laid on independent railroads in other States constituted a prior charge in equity upon the specific security of the consolidated mortgage upon the Richmond and Danville Railroad in Virginia.

ELEVENTH. The Circuit Court of Appeals decided erroneously in affirming the judgment of the Circuit Court requiring the bondholders to pay full interest upon the claim of the petitioner.

TWELFTH. The Circuit Court of Appeals decided erroneously in decreeing that the purchase by the general creditor receivership of steel rails from the appellee constituted such a diversion of the receivership income as equitably entitled the petitioner receiving such diverted income to be paid in addition an ante-receivership debt out of the sale proceeds.

Your petitioner exhibits as a part of this application a certified copy of the record, decree of affirmance and opinions of the said Circuit Court of Appeals.

The premises considered, petitioner prays that this Honorable Court will grant its writ of *certiorari* directed to the Circuit Court of Appeals for the Fourth Circuit, requiring that the record of said intervention cause in the said Court and its decree of affirmance thereof be certified to this Court, and that this Honorable Court will, thereupon proceed to correct the errors complained of, reverse the said decree and remand said cause, and give to your petitioner such other and further relief as

the nature of the case may require and to the Court may seem proper in the premises.

SOUTHERN RAILWAY CO.,
Petitioner.

HENRY CRAWFORD,
WILLIS B. SMITH,
Solicitors.

STATE, CITY AND COUNTY OF NEW YORK, ss. :

Before the undersigned, a notary public, personally comes SAMUEL SPENCER, president of the Southern Railway Company, petitioner, who, being duly sworn, deposes and says that the matters stated in the foregoing petition for *certiorari* are true as therein set forth to the best of his knowledge, information and belief.

Sworn to and subscribed be- }
fore me this twelfth day }
of December, 1896.